TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1926

No. 258

GEORGE D. PROVOST AND CORNELIUS W. PROVOST, COPARTNERS, COMPOSING THE FIRM OF PROVOST BROS. & CO., APPELLANTS,

vs.

THE UNITED STATES

APPEAL FROM THE COURT OF CLAIMS

FILED JANUARY 31, 1927

(29,682)

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INDEX

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., JUNE 30, 1925

[fol. 1] **IN THE COURT OF CLAIMS**

No. B-112

GEORGE D. PROVOST and CORNELIUS W. PROVOST, Copartners, Composing the Firm of Provost Bros. & Co., Claimants,

v.

THE UNITED STATES

I. PETITION—Filed June 2, 1922

To the Honorable the Court of Claims:

The claimants respectfully represent:

1. At all the times herein mentioned, claimants were and still are copartners doing business as stockbrokers under the firm name of Provost Bros. & Co., with their office and principal place of business at 20 Broad Street, in the Borough of Manhattan, City of New York, State of New York, and at all such times the claimant, Cornelius W. Provost, was a member of the New York Stock Exchange and the firm of Provost Bros. & Co. was registered with said Exchange.

2. While the Revenue Acts of 1917 and 1918 were in force, to wit: on various dates between December 1, 1917, and May 31, 1920, claimants, in the regular and ordinary course of their business, loaned stock to various other stockbrokers who borrowed the stock to make deliveries on short sales of similar stock which they had made in fulfillment of orders received from customers. Claimants affixed and cancelled the stamps to the "loan tickets" used to evidence the transaction, which "loan tickets" claimants delivered to the [fol. 2] borrowing brokers. On various dates during said period, claimants, in the regular and ordinary course of their business, returned stocks to various other stockbrokers, which stocks claimants had previously borrowed from said other stockbrokers to make deliveries on short sales of similar stocks which they had made in fulfillment of orders received from customers. Claimants affixed and cancelled the stamps to the "borrowed stock returned tickets" used to evidence the transaction and which claimants delivered to the lending brokers. By a "short sale" is meant a sale or contract for the sale of stock which the seller is not in a position to deliver at the time of making the sale or contract.

3. That neither of said Acts of Congress nor any other statute of the United States required or provided that the claimants should pay a tax on account of the lending of said shares of stock or on account of the returning of said shares of stock which had been borrowed, but that, nevertheless, the Commissioner of Internal Revenue on or about March 30, 1918, in Treasury Decision 2685 ruled and announced that the lending of such shares of stock and the

returning of such borrowed shares of stock was subject to the tax imposed by Sections 800 and 807, Schedule A, Subdivision 4, Title VIII of the War Revenue Act of October 3, 1917, and that thereafter the Collector of Internal Revenue for the Second District of New York forced and compelled the claimants to pay taxes under said provisions of the Revenue Act of 1917 and under Sections 1100 and 1107, Schedule A, Subdivision 4, Title XI of the Revenue Act of 1918, on account of stocks loaned and borrowed stocks returned.

4. The taxes paid by claimants during said period as a result [fol. 3] of said rulings and act of the Commissioner of Internal Revenue and the Collector of Internal Revenue for the Second District of New York, were as follows:

	Dec. 1, 1917, to July 31, 1918	Aug. 1, 1918, to May 31, 1920	Total
Stocks loaned.....	$50.00	$84.00	$134.00
Borrowed stocks returned..	1,246.50	1,964.26	3,210.76
Total	$1,296.50	$2,048.26	$3,344.76

5. Claimants paid said taxes under protest and duress and solely in order to avoid the pains and penalities provided by law in the case of non-payment of taxes demanded by a Collector of Internal Revenue.

6. The contract and agreement under which claimants loaned stock as aforesaid in the instances in which they did loan stock and the contract and agreement under which claimants returned stock as aforesaid, which they had previously borrowed, in the instances where they returned borrowed stock, was a contract and agreement to act in accordance with and to be bound by the following customs (expressed in the present tense) which were applicable to all of the transactions herein referred to, viz:

(a) The borrowing broker agrees to return the stock to the lending broker on demand.

(b) The borrowing broker deposits with the lending broker as security when the loan of the stock is made, the full market price of the stock and thereafter while the loan continues the sum in the hands of the lending broker is kept, by payments back and forth between the borrowing and lending brokers, at the market price of the stock as it fluctuates. These items are called "mark-ups" (market up) and "mark-downs" (market down).

[fol. 4] (c) The lending broker has the use of the money deposited with him while the loan lasts and accordingly pays the borrowing broker interest at such rate as is agreed upon between them from day to day. The usual rate is about the same as the prevailing rate for "call loans" of money. The borrowing broker, if he is obliged to do so to get the stock, may waive the payment of

interest. The stock is then said to be loaned "flat." If there is an unusual demand for the stock, the borrowing broker may even have to pay a cash consideration to get the loan. The amount so paid is known as a "premium."

(d) If any dividends are declared on the stock during the existence of the loan, the borrowing broker pays the dividends to the lending broker. All rights, privileges and increase of the stock become the property of the lending broker. If any assessments are levied, the lending broker pays the amount thereof to the borrowing broker.

(e) Stockbrokers send reports to their customers on the day a purchase or sale of stock is made for the customer notifying the customer with reference to each purchase or sale, the fact that it was made, the date, the number and kind of shares bought or sold, the price, the name of the broker from whom the stock was purchased or to whom it was sold and the time of the purchase or sale. Stockbrokers on making a short sale for a customer send a similar report of the sale to the customer for whom the short sale is made, without specifying that the sale is a short sale. Stockbrokers do not send any reports to their customers with reference to stock borrowed to carry out a short sale nor with reference to the return of borrowed stock, either during the continuance of or on the completion of a short sale. Stockbrokers do not communicate with their customers [fol. 5] with reference to stocks loaned, borrowed or returned in connection with short sales and do not notify the customers of anything in connection therewith, except with reference to margin, dividends, assessments, interest and premiums, if any.

(f) Neither the lending nor the borrowing broker charges any commission to his customer in connection with the lending or borrowing of stock nor the return of borrowed stock.

(g) The lending and borrowing brokers act as principals in connection with the loan and return of the stock. They deal with one another in their own names, the names of their customers do not appear in the transactions between the brokers. The names of the customers of each broker appear in the broker's own books, but the names are not disclosed to the other brokers in the transaction.

(h) The transaction is called and considered by all the parties thereto, including the stockbrokers and their customers, a "borrowing" of stock and not a sale or transfer thereof, and the stock so loaned is generally known and termed in the business as "loaned stock" or "borrowed stock" and when returned is generally known and termed in the business as "returned stock" or "borrowed returned stock."

7. In every case in which stock was borrowed as aforesaid, the following federal taxes were paid in addition to the taxes paid on the loan and on the return of borrowed stock, viz: (1) A tax was paid by the borrowing broker on the "short" sale made by him; and (2) On the repurchase of the stock by the borrowing broker for the

purpose of returning the "borrowed" stock, the broker who sold the stock to him paid a similar tax. By reason of the requirement of the Commissioner and the Collector of Internal Revenue aforesaid, [fol. 6] four federal taxes were paid in each and every instance in order to effectuate a short sale.

8. That heretofore and on or about August 17, 1920, the claimants duly made and filed with the Commissioner of Internal Revenue their appeal for the refund of said amount paid as aforesaid, according to the provisions of law in that regard and the regulations established by the Secretary of the Treasury pursuant thereto, and that more than six months has elapsed since the date of said appeal and no decision thereon has been made by said Commissioner of Internal Revenue. No other action than as aforesaid has been had upon this claim in Congress or by any of the Departments.

9. The claimants are the sole owners of this claim and the only persons interested therein; and no assignment or transfer of this claim or any part thereof, or interest therein, has been made.

10. The claimants are justly entitled to the amount herein claimed from the United States after allowing all just credits and offsets. The claimants are citizens of the United States and have at all times borne true allegiance to the Government thereof and they have not nor has any of them in any way voluntarily aided, abetted or given encouragement to rebellion against the said Government; and the claimants believe the facts as stated in this petition to be true.

And the claimants claim the sum of $3,344.76 and interest.

Goldman & Unger, Attorneys for Claimants. Office and P. O. address: 120 Broadway, Manhattan, New York City, New York.

[fol. 7] Sworn to by George D. Provost. Jurat omitted in printing.

[fol. 8] II. General Traverse—Entered Aug. 2, 1922

No demurrer, plea, answer, counterclaim, set-off, claim of damages, demand, or defense in the premises, having been entered on the part of the defendant a general traverse is entered as provided by Rule 34.

III. Argument and Submission of Case—Oct. 21, 1924

On October 21, 1924, this case was argued by Mr. George W. Wickersham, for the plaintiffs, and by Messrs. Charles T. Hendler and Fred K. Dyar, for the defendant.

On October 22, 1924, the case was further argued by Mr. Charles T. Hendler, for the defendant. Mr. George W. Wickersham, was heard in reply for plaintiffs, and the case was submitted.

[fol. 9] **Findings of Fact, Conclusion of Law, and Opinion of the Court by Booth, J.**—Entered December 1, 1924

This case having been heard by the Court of Claims on a stipulation of facts by the parties, signed on behalf of the plaintiffs by their attorneys, Goldman & Unger, and on behalf of the defendant by Robert H. Lovett, Assistant Attorney General, the court adopts said stipulation as its

FINDINGS OF FACT

I

At all the times herein mentioned plaintiffs were and still are copartners, doing business as stockbrokers under the firm name of Provost Bros. & Co., with their office and principal place of business at 20 Broad Street, in the Borough of Manhattan, city of New York, State of New York, and at all such times the plaintiff, Cornelius W. Provost, was a member of the New York Stock Exchange, and the firm of Provost Bros. & Co. was registered with said exchange.

II

Under date of March 30, 1918, the Commissioner of Internal Revenue made the following ruling (Treasury Decision No. 2685):

Treasury Department,

Office of Commissioner of Internal Revenue,

Washington, D. C.

To Collectors of Internal Revenue and others concerned:

In accordance with an opinion from the Attorney General, dated March 23, 1918, it is held that the transfer of shares or certificates of stock in any association, company, or corporation made by the person loaning stock to another borrowing the stock to effect a sale, and also the transfer of shares or certificates of stock from a borrower returning them to a lender in fulfillment of the borrower's obligation to buy in and return stock, are both subject to the tax imposed by sections 800 and 807, schedule A, subdivision 4, Title VIII, of the war revenue act of October 3, 1917. In a so-called short-sale trans-[fol. 10] action there are, therefore, four taxable sales or transfers: (1) The sale of stock by the person making the short sale; (2) the transfer from the lender of stock to the person making the short sale, so that he may make delivery of the stock sold; (3) the purchase by the borrower of stock to return to the lender; (4) the transfer from the borrower to the lender of shares to replace those borrowed.

Daniel C. Roper, Commissioner of Internal Revenue.

Approved March 30, 1918. W. G. McAdoo, Secretary of the Treasury.

III

By a "short sale" of stock is meant a sale or contract for the sale of stock which the seller does not deliver to the broker who is employed to make the sale.

IV

Some of the short sales referred to herein were made by plaintiffs and some by other stockbrokers. They were made by the various stockbrokers in their own names in fulfillment of orders received from customers.

V

The short sale of stock was evidenced by a memorandum of sale, or "sales ticket," delivered by the selling broker to the buying broker, and to which the selling broker affixed Federal stock transfer stamps and canceled the stamps.

VI

Rule XXIII of the New York Stock Exchange requires the broker who sells stock for a customer on the New York Stock Exchange to make delivery of the stock the following business day. There is a custom to a similar effect with reference to stock sold elsewhere than on the New York Stock Exchange. Said rule and custom are applicable to short sales. Said rule of the New York Stock Exchange reads as follows:

"Article XXIII.—Bids and Offers

"Sec. 3. Bids and offers may be made only as follows:

* * * * * * *

"(b) 'Regular way,' i. e., for delivery upon the business day following the contract; * * *

"Bids and offers made without stated conditions shall be considered to be in the 'Regular way' * * *."

VII

Since in a short sale the customer does not deliver the stock to his broker, and it being necessary under said rule and custom for the broker to make delivery of such stock on the next succeeding business day, it is the custom of stockbrokers to borrow similar stock from other brokers in order to make delivery in accordance with the said rule and custom, respectively.

[fol. 11]

VIII

On a short sale made by plaintiffs they borrowed the stock from other stockbrokers to make delivery. On a short sale made by other brokers, such brokers borrowed the stock from plaintiffs to make delivery.

IX

Federal stock transfer stamps at the rate of 2 cents for each $100 face value or fraction thereof of the stock loaned and/or returned were cancelled when the stock was loaned or returned during the period hereinafter mentioned. The loan of stock was evidenced by a "loan ticket," to which the broker loaning the stock affixed and cancelled the stamps. The return of stock was evidenced by a "borrowed stock returned ticket," to which the broker returning the stock affixed and cancelled the stamps.

X

When the loan of stock is made, the broker borrowing the stock deposits the full market price of the stock with the broker lending the stock as security, and thereafter, during the continuance of the loan, the sum in the hands of the broker lending the stock is kept, by payments back and forth between the two brokers, at the market price of the stock as it fluctuates. These items are called "mark ups" (market up) and "mark downs" (market down).

XI

The broker lending the stock has the use of the money deposited with him while the loan lasts, and pays the broker borrowing the stock interest at such rate as is agreed upon between them from day to day. The usual rate is about the same as the prevailing rate for "call loans" of money. The broker borrowing the stock, if he is obliged to do so in order to get the stock, may waive the payment of interest. The stock is then said to be loaned "flat." If there is an unusual demand for the stock, the borrowing broker may even have to pay a cash consideration in order to obtain the stock. The amount so paid is known as a "premium."

XII

If any dividends (whether they be cash dividends or stock dividends) are declared on the stock during the existence of the loan, the amount thereof is paid by the broker borrowing the stock to the broker lending it. As between the two brokers, all rights and privileges in connection with the stock are and remain the property of the broker lending the stock as against the broker borrowing it. If any assessments are levied on the stock during the existence of the loan the amount thereof is paid by the broker lending the stock to the broker borrowing it. As between the two brokers, all burdens in connection with the stock rest and remain with the broker lending the stock as against the broker borrowing it.

[fol. 12]

XIII

Stockbrokers, on making a short sale for a customer, send a report of the sale to the customer for whom the short sale is made, without

specifying that the sale is a short sale. Stockbrokers do not send any reports to their customer with reference to stock borrowed to carry out a short sale nor with reference to the return of borrowed stock, either during the continuance of or on the closing out of a short sale. Stockholders do not communicate with their customer with reference to stocks loaned, borrowed, or returned in connection with a short sale, and do not notify the customer of anything in connection therewith, other than with reference to margin, dividends, assesments, interest, all stock transfer stamp taxes charged to the customer's account in connection with the "short" sale transaction, and premiums, if any.

XIV

Neither the lending nor the borrowing broker charges any commission to his customer in connection with the lending or borrowing of stock or the return of borrowed stock.

XV

When the customer who has sold "short" desires to cover his short sale and thus close the transaction his broker buys similar stock from another broker and delivers the stock thus purchased to the broker who loaned the stock, and receives back from him the deposit of cash, subject to the adjustment of any necessary differences. Where a broker buys stock to cover a short sale for a customer Federal stock transfer stamps are affixed to the "sales ticket" and cancelled by the selling broker, and the broker borrowing the stock affixes Federal stock transfer stamps to the "borrowed stock returned ticket" and cancels the stamps.

XVI

Either the broker lending stock or the broker borrowing it to make delivery on a "short" sale may terminate the loan on demand. If the broker lending the stock "calls" the loan before the customer of the broker borrowing the stock desires to close the transaction, the latter broker borrows similar stock from another broker and returns it to the broker who loaned the stock. There may be many such substitutions before the customer who has sold "short" desires to close the transaction, and in the case of each such substitution the broker lending the stock affixes Federal stock transfer stamps to the "loan ticket" and cancels the stamps, and the broker borrowing stock affixes Federal stock transfer stamps to the "borrowed stock returned ticket" and cancels the stamps.

XVII

The lending and borrowing brokers in connection with the loan and return of stock deal with one another in their own names. The [fol. 13] names of their customers do not appear in the transactons

between the brokers. The names of the customers of each broker appear in the broker's own books, but the names are not disclosed to the other brokers to the transaction.

XVIII

The transaction of borrowing and lending stock as herein described is known and termed in the stock brokerage business as a "borrowing of stock." The stock so loaned is generally known and termed in the business as "loaned stock" and "borrowed stock," and when returned is known and termed in the business as "returned stock" or "borrowed stock returned."

XIX

Where plaintiffs loaned stock this claim is only for stamps canceled by them when they loaned the stock, and does not include stamps canceled by the broker who borrowed the stock when the latter returned the stock to plaintiffs. Where plaintiffs borrowed stock this claim is only for stamps canceled when they returned the borrowed stock, and does not include the stamps canceled by the lending brokers when plaintiffs borrowed the stock.

XX

This claim is limited to stamps used and canceled by plaintiffs in connection with stocks loaned to or borrowed from other brokers (commonly called "interoffice borrowings") and does not include stamps used in connection with stocks loaned by plaintiffs themselves to their customers (commonly called "intraoffice borrowings").

XXI

While the revenue acts of 1917 and 1918 were in force, to wit, on various dates between December 1, 1917, and May 31, 1920, plaintiffs, in the regular and ordinary course of their business, loaned stock to various other stockbrokers, who borrowed the stock to make deliveries on short sales of similar stock which they had made in fulfillment of orders received from customers. Plaintiffs affixed the stamps to the "loan tickets" and canceled the stamps. On various dates between December 1, 1917, and May 31, 1920, plaintiffs, in the regular and ordinary course of their business, returned stock to various other stockbrokers, which stock plaintiffs had previously borrowed from said other stockbrokers to make deliveries on short sales of similar stock which they had made in fulfillment of orders received from customers. Plaintiffs affixed the stamps to the "borrowed stock returned tickets" and cancelled the stamps.

XXII

On and after April 1, 1918, plaintiffs, pursuant to Treasury Decision No. 2685, affixed and cancelled Federal stock transfer stamps [fol. 14] on "loan tickets" and on "borrowed stock returned tickets" in the following amounts on the following transactions:

	Dec. 1, 1917, to July 3, 1918	Aug. 1, 1918, to May 31, 1920	Total
Stocks loaned	$50.00	$84.00	$134.00
Borrowed stocks returned	1,246.50	1,964.26	3,210.76
Total	1,296.50	2,048.26	3,344.76

XXIII

In each case in which a certificate of stock was delivered—from the selling broker to the buying broker, from the broker lending the stock to the broker borrowing it, and, in the case of returned borrowed stock, from the broker returning the stock to the broker lending it—such certificate was assigned in blank by the stockholder of record on the books of the corporation.

XXIV

The affixing and canceling of the stamps, the value of which is herein claimed, was done pursuant to the ruling of the Commisioner of Internal Revenue hereinbefore set forth.

XXV

The customs applicable to the purchase of stock-transfer stamps and charging the cost thereof to the accounts of customers on whose order the various short sales were made were as follows (expressed in the present tense):

(a) Stockbrokers, from time to time, in order to meet their general business requirements, purchase supplies of Federal stock transfer stamps from the representative of the Treasury Department of the United States.

(b) Stockbrokers pay with their own funds for all such stamps.

(c) Customers do not give their brokers money for stamps in advance of the purchase or use of the stamps by the brokers.

(d) Stockbrokers subsequently use the stamps from time to time as occasion arises in the course of their business, and in the regular course of their business use some of the stamps in connection with "loaned" and "borrowed returned" stock.

(e) Stockbrokers affix the stamps to the proper documents, and stamp the initials of their firm name on said stamps and the re-

spective dates on which they are used, and cut or perforate the stamps in a substantial manner so that the stamps can not be again used.

(f) The brokers' customers do not buy or affix and cancel any of the stamps used on short sales made on their behalf—neither on the "sales ticket," on the "loan ticket," nor on the "borrowed stock returned ticket."

(g) The broker borrowing the stock repays to the broker lending the stock the cost of stamps affixed and canceled by the lending [fol. 15] broker on the "loan tickets," and the broker borrowing the stock in turn charges the amounts so paid to the accounts of the customers for whom he makes the short sales and borrows the stock. The broker borrowing the stock also charges to his customers' accounts the costs of stamps affixed and canceled on "borrowed stock returned tickets."

XXVI

Purchase and sales of stocks, borrowing and lending stock, and returning of stocks borrowed, in the case of all active securities listed on the New York Stock Exchange, are cleared through the stock Exchange Clearing House—that is, these various transactions are evidenced by "sales tickets," "loan tickets," and "borrowed stock returned tickets," respectively, which are cleared on balances through the clearing house. Usually on a short sale delivery of the certificate is not made to or received from the broker with whom the trade was made.

XXVII

On or about August 17, 1920, the plaintiffs filed a claim with the Commissioner of Internal Revenue for the refund of said amount of $3,344.76, and said claim for refund has never been acted upon by the Commissioner of Internal Revenue and was pending more than six months before the filing of the peition herein. No other action than as aforesaid has been had on this claim in Congress or by any of the departments.

XXVIII

The said claim was not accompanied by the canceled stamps. When plaintiffs loaned stock they delivered the "loan tickets," with the canceled stamps affixed thereon, to the brokers who borrowed the stock. When plaintiffs returned to other brokers stock which plaintiffs had previously borrowed from such other brokers, plaintiffs delivered the "borrowed stock returned tickets," with the canceled stamps affixed thereon, to such other brokers.

Conclusion of Law

Upon the foregoing findings of the fact the court decides, as conclusion of law, that the plaintiffs are not entitled to recover.

It is therefore adjudged and ordered that the plaintiffs' petition be and the same is hereby dismissed. Judgment is awarded against the plaintiff in favor of the defendant for the cost of printing the record in this case, the amount thereof to be entered by the clerk and to be by him collected according to law.

OPINION—Filed Dec. 1, 1924

BOOTH, Judge, delivered the opinion of the court.

The importance of this case is magnified by the number dependent upon its decision, for it is manifestly one of a large class. The facts are not disputed, a stipulation covering practically all the essential ones being in the record.

[fol. 16] The plaintiffs are copartners engaged in the brokerage business in New York City under the firm name of Provost Brothers and Company. Through proper connections with the New York Stock Exchange they accept and execute orders from customers for the sale of stock short, or, as familiarly known, short sales of stock. The stipulated facts disclose the following steps involved in a short sale of stock: X, the customer, gives to Y, his broker, an order to sell 100 shares of a certain stock which neither X nor Y owns or possesses, and which, of course, X can not deliver to Y. At the time the sale is made Y accepts the order and sells 100 shares of the designated stock to S.

The rules of the stock exchange require the delivery to the purchaser of all stock purchased on the day following the purchase. Therefore, in order to comply therewith and make delivery, Y procures the 100 shares from M, another broker, and delivers the same to S, at the time being required by M to deposit with him a sum of money equal to the market value of the stock so procured and maintain said deposit on a par with the market value of the same from day to day so long as the transaction continues. If the stock advances Y must increase the deposit; if it declines M is required to pay the amount of the same to Y. At all events the amount of the deposit in accord with the market value of the stock must be maintained M may demand of Y a return of an equal amount of stock at any time he chooses, and Y is obligated to so return it. M, if the agreement so provides, may be required to pay interest on the deposited funds at a rate agreed upon. M may, if he chooses, decline to pay any interest whatsoever and instead exact a premium for the loan of the stock. The question of loaning and the terms of the loan rest with M. Finally, X, the customer of Y, desires to close the short sale, i. e., "cover his short sale." Y then goes into the open market and purchases 100 shares of stock of the same kind he procured from M, delivers it to M, and reclaims his deposit, settling afterward with his customer. The transaction is obviously speculative, and in so far as its consummation is concerned the customer X is not a party to the agreement between Y and M.

In the course of business and in accord with the rules and customs of the exchange the transfer of shares of stock from what is known

as the lending broker to the borrowing broker is accomplished by the exchange of "loan tickets" and "borrowed stock returned tickets," these being no more than written memoranda of the transaction. Actual delivery is accomplished by the balanced transactions of the brokers through the Stock Exchange Clearing House each day. The Commissioner of Internal Revenue, in construing the Revenue Acts of 1917 and 1918, after repeated conferences, followed by an opinion of the Attorney General, ruled in Treasury Decision No. 2685 that the plaintiffs, as well as all others similarly engaged, must affix to the memoranda, i. e., the tickets, and cancel revenue stamps of the requisite amount in every instance of lending and the return of borrowed stock to effectuate a short sale thereof. This the plaintiffs did to the amount of $3,344.76, and this is the sum involved in this proceeding, the parties stipulating that the total sum represents the amount expended for revenue stamps, some of which were affixed to the loan-stock tickets and the balance to borrowed stock-return tickets.

[fol. 17] It is conceded that under the revenue laws stamps are required to be affixed and canceled in sales of stock short when the borrowed stock is delivered by the borrowing broker to the purchaser S, and likewise when the stock is purchased by the borrowing broker to be returned to the lending broker M. No question as to transfer of title is raised as to these two transactions. The challenge of illegality goes exclusively to the intermediate steps employed by the borrowing broker to procure the stock in order to fulfil his sale thereof and to the instances where stock is loaned for a similar purpose. As to the transaction between Y and M, to which X the customer of Y is not a party, the plaintiffs contend that from its very nature the legal relationship of pledgor and pledgee exists, and a fortiori title to the stock was not transferred but remained in the lender of the stock, and its mere physical delivery to the borrower of the stock was not such a delivery of the same as the revenue laws contemplate.

So far as this discussion is affected the pertinent provisions of the Revenue Acts of 1917 and 1918 are the same. Paragraph 4 of Schedule A, Title VIII of the Revenue Act of 1917, 40 Stat., 300, 319, 322, provides as follows:

"Schedule A—Stamp Taxes

* * * * * * *

"4. Capital stock, sales or transfers: On all sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares or certificates of stock in any association, company, or corporation, whether made upon or shown by the books of the association, company, or corporation, or by any assignment in blank or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock or not, on each $100 of face value or fraction thereof, 2 cents, and where such shares of stock

are without par value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share, unless the actual value thereof is in excess of $100 per share, in which case the tax shall be 2 cents on each $100 of actual value or fraction thereof: Provided, That it is not intended by this title to impose a tax upon an agreement evidencing a deposit of stock certificates as collateral security for money loaned thereon, which stock certificates are not actually sold, nor upon such stock certificates so deposited: Provided further, That the tax shall not be imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased same, but such deliveries or transfers shall be accompanied by a certificate setting forth the facts: Provided further, That in case of sale where the evidence of transfer is shown only by the books of the company the stamp shall be placed upon such books; and where the change of ownership is by transfer of the certificate the stamp shall be placed upon the certificate; and in cases of an agreement to sell or where the transfer is by delivery of the certificate assigned in blank there shall be made and delivered by the seller to the buyer a bill or memorandum of such sale, to which the [fol. 18] stamp shall be affixed; and every bill or memorandum of sale or agreement to sell before mentioned shall show the date thereof, the name of the seller, the amount of the sale, and the matter or thing to which it refers. Any person or persons liable to pay the tax as herein provided, or anyone who acts in the matter as agent or broker for such person or persons who shall make any such sale, or who shall in pursuance of any such sale deliver any stock or evidence of the sale of any stock or bill or memorandum thereof, as herein required, without having the proper stamps affixed thereto with intent to evade the foregoing provisions shall be deemed guilty of a misdemeanor, and upon conviction thereof shall pay a fine of not exceeding $1,000, or be imprisoned not more than six months, or both, at the discretion of the court."

The enacting clause of the statute is free from ambiguity. Its terms are specific. The manifest legislative intent was to subject the ordinary and usual dealings in stock to the payment of the stamp tax imposed, except as to the transactions enumerated in the provisos. The language employed obviously extends, and was designed to extend, to "sales, or agreements to sell, or memoranda of sales or deliveries of or transfers of legal title to shares or certificates of stock." These words, when given their usual and customary meaning in the commercial world, are in nowise obscure, and it would be difficult indeed to have employed language conveying a plainer intent to reach the modus operandi of dealing in stocks, both on and off the stock exchange, than appears from a reading of the statute. If, then, the plaintiffs' claimed immunity from the payment of the tax is to prevail, it must appear that the steps involved in the procurement and return of the borrowed stock does not constitute in law a transfer of the title to the same "or deliveries of" the stock, for in all other respects the details of the transactions seem to come within the law. Selling short, as previously observed, is entirely a speculative trans-

action. One who sells short through a broker hazards a bargain on the decline of the market value of the stock sold. The customer knows, and of course the broker is fully conscious, of the necessity of procuring the stock to make delivery thereof. While the customer is not a party to the procurement of the stock, he knows, and it is notorious that one of the express duties of the broker is to procure the stock for this very purpose.

Selling short has long been an established custom of stock exchanges. The mode of meeting the requirements of the law with respect thereto has been in existence for many decades. It is an established trade, indulged in daily to a large extent, and it is indisputable that the intent and purpose, the vital and moving motive, for the transfer of stock from the lending to the borrowing broker, and vice versa, is to enable the one borrowing the stock to complete a sale of the identical stock borrowed by transferring the title of the stock borrowed to the purchaser. This is the very essence of the transaction. Bereft of this right and privilege to pass title to the stock borrowed the transaction itself would lapse into discontinuance. The parties to it so understand, and have for a long time, and in innumerable transactions put this construction on the created relationship. To effectuate this purpose and simplify the proceedings certificates of stock are indorsed in blank and thereby [fol.19] made negotiable. No lender of stock has ever questioned or even contemplated challenging the right and privilege of the borrowing broker to transfer to his purchaser the complete title and possession of the borrowed stock. This right is part of the consideration for the inter partes agreement contemplated by the parties themselves and indisputably established by the rules and regulations of the exchange, and carried into effect by trading arrangements and regularly established posts on the floor of the exchange where the lending and borrowing of stock to complete short sales is a firmly established stock transaction. It is true the borrower must return to the lender a like amount of stock, and enters into cash security to do that very thing, but the very fact that the borrower's obligation is limited to a return of a like amount of stock when called upon to do so is potent evidence of the intention of the parties to vest title in the tangible stock transferred and grant to the borrower the legal right to procure as best he may the necessary stock to take the place of the amount first transferred to him. As said by the Attorney General, 31 Op. Atty. Gen., 255, 258, "Shares of stock are fungible things, and their loan with an agreement to return things of the same class is the mutuum of Roman law, as to which no one can doubt that title passed from the lender to the borrower and vice versa."

In addition to what has been said, the revenue acts of 1917 and 1918 apply specifically to the title of the tangible thing transferred. Stamps must be affixed to the memoranda, to the agreement or to the certificate when any one of these instruments passes from one to another in ownership, irrespective of the agreement between the parties as to reciprocal rights and obligations growing out of the transaction. It is a tax upon the instrument itself, and it may not for a moment be doubted that the transfer of the certificate of

stock from the lending to the borrowing broker vests in the latter by the very terms of the agreement complete legal title to the certificate, a title sufficient in law to enable him to convey it to another free from all claims and demands whatsoever of the lender, and which the lender voluntarily parts with and never receives in return. The agreement of the borrower to maintain the status quo of the lender as the real owner of the stock and pay to him accrued dividends thereon is manifestly an obligation assumed for the transfer of the stock to the borrower. The latter does not, nor does he pretend to collect dividends from the corporation issuing the stock; he necessarily pays them from his private funds. Likewise, the lender assumes in the agreement the liabilities of an owner of stock and agrees to pay all assessments, etc., but as between the corporation issuing the stock and the lender, no liability attaches to the latter. These assumed obligations are contractual. The title to the stock itself, or the certificate evidencing ownership thereof, has passed from both the parties to this contract and is vested in the purchaser. He, in reference to the ownership of the stock, collects the dividends from the corporation and is subject to the liabilities of a stockholder of the corporation. This, it seems to us, is clearly what the Congress regarded as a legitimate source of revenue and by the terms of the statute exacted the stamp tax whenever the title to the instrument passed from the owner to another.

[fol. 20] When one purchases stock through a broker on a margin the Supreme Court has said that the legal relationship between the broker and his customer is that of pledgor and pledgee. Richarson v. Shaw, 209 U. S., 365; Gorman v. Littlefield, 229 U. S., 19. The plaintiffs stress this fact, and seek to liken a sale of stock short with a purchase of stock on a margin. In both the above cases no revenue legislation was involved. The controversy was between a trustee in bankruptcy of the broker's estate and the purchaser of the stock on a margin from the bankrupt broker previous to his bankruptcy, and as the Attorney General in his opinion said, "as against the broker and his trustee in bankruptcy an equitable right in rem to stock in the broker's possession of the same species as that dealt in between them" prevailed. In delivering the opinion of the court in Richardson v. Shaw, supra, at p. 375, Mr. Justice Day says: "The position of the broker is twofold. Upon the order of the customer he purchases shares of stock desired by him. This is a clear act of agency. To complete the purchase he advances from his own funds, for the benefit of the purchaser, ninety per cent of the purchase money. Quite as clearly he does not in this act as an agent, but assumes a new position. He also holds or carries the stock for the benefit of the purchaser until a sale is made by the order of the purchaser or upon his own action. In thus holding or carrying he stands also upon a different ground from that of a broker or agent whose office is simply to buy and sell. To advance money for the purchase, and to hold and carry stocks, is not the act of the broker as such. In doing so he enters upon a new duty, obtains other rights, and is subject to additional responsibilities. In my judgment the contract between the parties

to this action was in spirit and effect, if not technically and in form, a contract of pledge."

In other words, carrying a customer on a margin is the equivalent of loaning money upon stock as collateral for a loan. This, it seems to us is essentially different from executing for another the sale of stock which one does not own or possess. In one instance the broker purchases for another certain shares of stock for his customer advancing from his own funds eighty or ninety per cent of the purchase price, retaining possession of the stock, and exercising certain conferred rights with respect thereto until it is paid for and the deal closed. In the case of selling short the broker undertakes to complete the sale for his customer, and, unlike the margin transaction, he is not required from his own funds to maintain the deposit required by the lender to its full extent, for he receives as a credit toward this amount the purchase money which the purchaser of the stock pays him on delivery, and thus may or may not be required to invest his own funds in the transaction at all. In any event, under the terms of the agreement the broker may not even be required to part with any greater sum of his own funds than the difference between what he receives from his vendee and the market value of the borrowed stock. If the stock declines the broker obtains the use of so much of his customer's money. If it advances he must post the difference in market value with the lending broker. This, it seems to us, is an essential difference in character, so far as the borrowing broker is concerned, between a long sale on a margin and [fol. 21] a short sale of stock. The borrowing broker has no stock as collateral; he has the funds of his customer to buy the same, and these funds he uses to procure the stock from the lending broker, and to repurchase as the necessities of the case require. Stripped of its technical refinements and considered free from all extraneous surroundings the established business of loaning and borrowing stock for the fulfillment of short sales of stock is sui generis in character, and not to be assimilated with other well known and easily recognized commercial transactions bearing some analogy thereto. The transaction is to be considered in the light of what it really is, the contract to be construed according to the real intention of the parties and effect given to that intention as reflected by the relationship created and the vital purpose to be accomplished.

The indispensable requirement of an actual delivery of stock sold short by brokers creates a market for borrowed stock, a market so extensive as to develop a settled and exclusive business for this identical purpose, a business conducted for profit and governed by the rules of the stock exchange. A station on the floor of the exchange, as before observed, is set apart where dealings in borrowed stock obtain, and hours are fixed within which the lender and borrower may appear and make terms as to the loan. The lender of stock concededly may exact a premium for its loan, decline to pay interest on the deposited funds, and otherwise adjust the terms of the transaction in accord with his own disposition in this respect. Transactions of this character are cleared through the Stock Exchange Clearing House, and every feature of the transaction clearly

and unmistakably indicates a mutual understanding and long settled conception of reciprocal rights accruing to the parties thereto. The lender knows that he passes to his borrower title to the stock transferred, for he knows the purpose of the borrowing is to complete a short sale thereof. The borrower knows he acquires title to the stock and that he must eventually go into the open market and purchase from another stock of like description to make good his agreement. Both parties to the agreement know that until this is done neither the lender nor the borrower has in his possession or ownership the stock passing from the one to the other. The tangible thing itself has passed in ownership and title from both, and this in our opinion is what the revenue laws intended to tax. Whenever title passed and transfer thereof was an indispensable concomitant of the agreement of the parties the stamps must be affixed to the instrument representing the transfer, and canceled, irrespective of the contractual rights of the parties to the agreement voluntarily entered into. The law taxed what actually happened, the instrument representing change of ownership, and not the contract of the parties with respect thereto. Certificates of stock, like fungible goods circulating from one to another under the rules governing selling short, pass in ownership with the same effect and result as any other negotiable instrument.

We are alone concerned with the devolution of title of the specific thing itself. If by the terms of the agreement title to the subject matter passed, the law taxes its transfer, and the payment of the tax may not be escaped, notwithstanding the mutual obligations of the parties to the agreement by which title passed. In one instance rights are to be determined by the contract; with respect to the [fol. 22] Government and the laws of Congress the transaction is to be viewed in the light of actualities and the principles of law applicable thereto. This we think is expressly accentuated by that provision of the taxing act which expressly inhibits the courts from consideration of beneficial interests so far as the holder of the stock is concerned. The tax, the statute says, must be paid on transfers of title "whether entitling the holder in any manner to the benefit of such stock or not."

The courts of New York, in two cases at least, have decided adversely to plaintiffs' contention. Travis v. Ann Arbor Co., 168 N. Y. S., 53; Bonbright Co. v. State, 151 N. Y. S., 35. In both cases State revenue legislation, in every essential respect similar to the laws here involved, were considered by the court, and the issue was precisely as it is here.

Again, it is said that the case falls clearly within the first proviso to the statutes. The argument to sustain this proposition is addressed to an alleged similarity between the deposit of stock as collateral security for money loaned, and the deposit of funds to secure the return of stock. To hold that the transaction covered by the findings comes within the meaning of the proviso would entail the necessity of doing violence to the ordinary and well established meaning of its words. The deposit of stock as collateral for money

loaned, a collateral loan, has a distinct and firmly established place in the commercial world. Bankers, business men and the entire commercial activity of the people have long since fixed the significance of the term, and we have no doubt as to the intention of Congress in the enactment of the proviso. Unmistakably it refers to the procurement of a loan of money from a bank or those engaged in loaning money, where the borrower receives his funds and deposits at the time such stock certificates with the lender as will assure the repayment of the loan. Such a transaction is wholly foreign to the modus operandi of speculation in stocks and bears no relation to it. Short sales of stock are provided for by the rules of the exchange, the transaction itself is primarily a purchase and sale of stock, and the very fact that Congress granted tax immunity to collateral loans is itself a most convincing argument that all other transactions in stocks were subject to the tax.

Finally, it is said that the proviso to the revenue act of 1921 clearly evinces an express intention to reject the construction put upon the acts of 1917 and 1918 by the Treasury Department. We assuredly recognize the rule, so emphatically asserted by the plaintiffs, that the court may examine all legislation in pari materia to ascertain legislative intent, where the statutes are ambiguous and the meaning obscure. It is an ancient canon of statutory construction. In this particular instance, however, it is manifestly inapplicable, because it encounters a state of facts which precludes resort thereto. Subsequently to the rulings of the Treasury Department, and at a time when in keeping with said ruling the tax here objected to was being collected, an effort was made in Congress to have the proviso which finally passed in 1921 injected into the act of 1918, and Congress declined to do it. Therefore, Congress, with full knowledge of the Treasury Department's construction and execution of the act of 1917, renacted it without change in 1918. It was not until three years later that Congress changed the policy of its ex- [fol. 23] cise legislation and exempted short sales from the payment of the tax. If Congress, fully cognizant of what was being done, and fully aware of an insistence for a change from the adopted construction, not only declines to make the change but reenacts the statute under criticism, we need not cite authorities to sustain the proposition that the effect is manifestly a congressional adoption of the construction adhered to. See Hearings Before Senate Finance Committee, on H. R. 12863, 65th Cong., 2d sess., p. 196; Senate Report No. 617, 65th Cong., 2d sess.; House Report No. 767, 65th Cong., 2d sess.

We have not ignored the many questions raised in the very able and exhaustive brief of counsel. To discuss them in detail would involve a tedious prolongation of this opinion. The defendant points out several technical objections to the maintenance of this suit. These, we think, are without merit. In any event, we are convinced that the case is one which may be concluded on its merits.

The petition is dismissed. It is so ordered.

Graham, Judge; Hay, Judge; Downey, Judge; and Campbell, Chief Justice, concur.

[fol. 24] V. JUDGMENT OF THE COURT—Filed Dec. 1, 1924

At a Court of Claims held in the City of Washington on the First day of December, A. D., 1924, judgment was ordered to be entered as follows:

The Court, upon due consideration of the premises, find in favor of the defendant, and do order and adjudge that the plaintiffs, as aforesaid, are not entitled to recover and shall not have and recover any sum in this action of and from the United States; and that the petition herein be and the same is hereby dismissed: And it is further ordered and adjudged that the United States shall have and recover of and from the plaintiffs, as aforesaid, the sum of Eighty-eight dollars and thirty-seven cents ($88.37), the cost of printing the record in this court, to be collected by the clerk, as provided by law.

By the Court.

[fol. 25] VI. PLAINTIFFS' APPLICATION FOR APPEAL—Filed December 17, 1924

From the judgment rendered in the above-entitled cause on the 1st day of December, 1924, in favor of the defendant, the claimants, by their attorneys, on the 17th day of December, 1924, make application for and give notice of an appeal to the Supreme Court of the United States.

Goldman & Unger, Attorneys for Claimant. Office & P. O. Address: 120 Broadway, Manhattan, New York City.

VII. ORDER OF COURT ALLOWING PLAINTIFFS' APPLICATION FOR APPEAL—Filed Jan 12, 1925

It is ordered by the Court this 12th day of January, 1925, that the plaintiffs' application for appeal be and the same is allowed.

[fol. 26] CLERK'S CERTIFICATE

[Title omitted]

I, F. C. Kleinschmidt, Assistant Clerk Court of Claims, certify that the foregoing are true transcripts of the pleadings in the above-entitled cause; of the argument and submission of case; of the findings of fact, conclusions of law and opinion of the court by Booth, J.; of the judgment of the court; of plaintiffs' application for appeal; of the order of the court allowing plaintiffs' application for appeal.

In testimony wrereof I have hereunto set my hand and affixed the seal of said Court at Washington City, this 15th day of January, A. D. 1925.

F. C. Kleinschmidt, Assistant Clerk Court of Claims. (Seal of the Court of Claims.)

Endorsed on cover: File No. 30,832. Court of Claims. Term No. 258. George D. Provost and Cornelius W. Provost, copartners, composing the firm of Provost Bros. & Co., appellants, vs. The United States. Filed January 26, 1925. File No. 30,832.